Litigation Avoidance: Steering Clear of Common Pitfalls

April 28, 2005

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This article is reprinted with permission from the April 2005, Volume 11, Issue 3 of Pittsburgh TEQ.

For most business owners, litigation is something to be avoided at all costs. While there is nothing inherently wrong with this view, avoiding lawsuits requires an upfront investment of time and money to be effective. As with any business risk, proper planning is critical. This article highlights some common business pitfalls to demonstrate how litigation can be avoided, or at the very least, minimized.

UNDOCUMENTED TERMS LEAVE ROOM TO ARGUE.

One of the most common mistakes is to fail to document transactions. Although e-mail has done wonders to create a paper trail, it has not solved all problems. Contractual disputes most often arise because the parties have different views about what they agreed to. When the terms of an agreement are memorialized in a clear and complete writing, the disagreement is short-lived. However, when the terms are left to be "proved" by recollections and scattered correspondence, memories become convenient and the resolution is bound to cost more than it should.

The more effectively a transaction is "papered" the less likely it is to end in litigation. An unhappy party is less likely to bring a lawsuit if the terms (including such things as remedies for breaking the agreement) are clearly spelled out. If a lawsuit is brought and the contract terms are clear and unambiguous, the suit is more likely to be resolved expeditiously. This advice applies to all sorts of contracts, including leases, supply and distribution agreements, licensing, joint ventures, etc.

THE PATH OF THE "PRODUCT" MAY LEAVE A WAKE OF LIABILITY.

Every business has a "product" – either tangible consumer goods, services or some combination of the two. Many businesses fail to invest the time to trace the path of their product, and consider where they may incur liability, and how that liability may be limited or eliminated. For example:

- Written agreements with suppliers should explicitly promise indemnification if the supplied materials cause a defect or loss.
- Tangible products must be adequately labeled, and accompanied by clear and understandable instructions, with satisfactory warnings to alert consumers to any inherent dangers.
- Contracts with distributors should clarify respective roles and obligations, including indemnification.

- Services should be provided pursuant to clear, comprehensive, signed agreements, which set forth schedules for performance and payment, procedures and remedies for default, etc.
- Warranties should be considered and carefully worded. Ideally, your product should go out into the world and generate profit without creating unanticipated future risks and liabilities.

UNPROTECTED TRADE SECRETS CREATE HIDDEN VULNERABILITIES.

Another common pitfall arises in the arena of confidential and proprietary information, as a result of hiring a competitor's employee or as a result of the departure of an employee to a competitor. Too often businesses wait until it is too late to deal with either scenario.

The time to protect your own confidential information is before key employees leave. Frequently, a business sues a departed employee and his or her new employer for such things as theft of trade secrets and violation of contracts. Only later does the business learn, for the first time, that it has not undertaken to reasonably protect its confidential information, making the lawsuit “un-win-able.”

Precautionary measures to protect confidential information might include:

- Restricting access to confidential information (i.e., through secure sites and passcodes);
- Ensuring that confidential information is not disclosed in advertising and marketing materials (such as Web sites);
- Using reasonable confidentiality agreements and covenants not to compete;
- Marking confidential information with appropriate legends; and
- Disseminating company-wide policies regarding confidentiality.

On the flip side, there are ways to hire a competitor's employees while minimizing the chance that you will be sued. Some of the methods that can be used include:

- Determining in the interview the existence of any contractual agreements that might prohibit the employee from the anticipated move;
- Advising your competitor of the potential hire to determine, in advance, objections/prohibitions to the hire;
- Advising new employees to abide by their contractual obligations with their former employers; and
- Where applicable, advising other employees of a new employee's confidentiality obligations to a former employer and setting up “information screens” accordingly.

DETAILS CAN MAKE A DIFFERENCE.

Finally, failure to mind the “details” – minutiae that seems unrelated to essential business function and are easily overlooked or postponed – is a pitfall that can cause large problems later.

- Get and keep complete, signed copies of all agreements. Unsigned copies are not conclusive proof of the deal.
- Read the “boilerplate” on the form purchase orders, invoices and other documents you exchange. If you don't agree with the terms, explicitly change the terms of the deal in writing. If you do nothing, you may be bound by those terms.
- Make sure that your insurance coverages are adequate for the type and size of your risks. Obtain confirmation that you have received “additional named insured” coverage any time it is promised to you in a contract.
- Maintain current and complete files on all important matters.
- Review all advertising for accuracy and truthfulness.

Sometimes litigation can be avoided through planning and careful practices. However, even when complete avoidance is impossible, good business practices can help to reduce the risks and increase the likelihood of success.

Alice Sacks Johnston contributed to this article.